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Is Financial Democracy a Click Away? Peer-to-Peer Lending and Beyond

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Microfinance Learning and Innovations After Hours Seminar

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Why Talk about Peer-to-Peer Lending?

- ❖ P2P lending is not a new concept (family and friends, ROSCAs)
- ❖ Internet has launched P2P lending to a new dimension, expanding communities beyond geographic boundaries & borrowing social networking ideas to create trust between strangers
 - Zopa UK first “domestic” P2P platform launched March 2005 (for-profit)
 - Kiva first platform geared towards microfinance (non-profit)
- ❖ Ultimate goal: link people with excess capital to those in need of capital, generally circumventing traditional banks, yet tapping into “retail” investors/lenders

By cutting out the middle man in financial intermediation, traditional banks, can P2P lending platforms help democratize the credit markets for lenders and borrowers?



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Overview of P2P Lending Market

Developed Economies

- ❖ Zopa UK launched in March 2005
- ❖ Now over 20 P2P platforms in 14 countries
- ❖ Another 10 are expected to be launched soon
- ❖ ~\$100 million lent on such platforms in 2007
- ❖ Online Banking Report estimates \$1 billion will be lent via P2P platforms by 2010

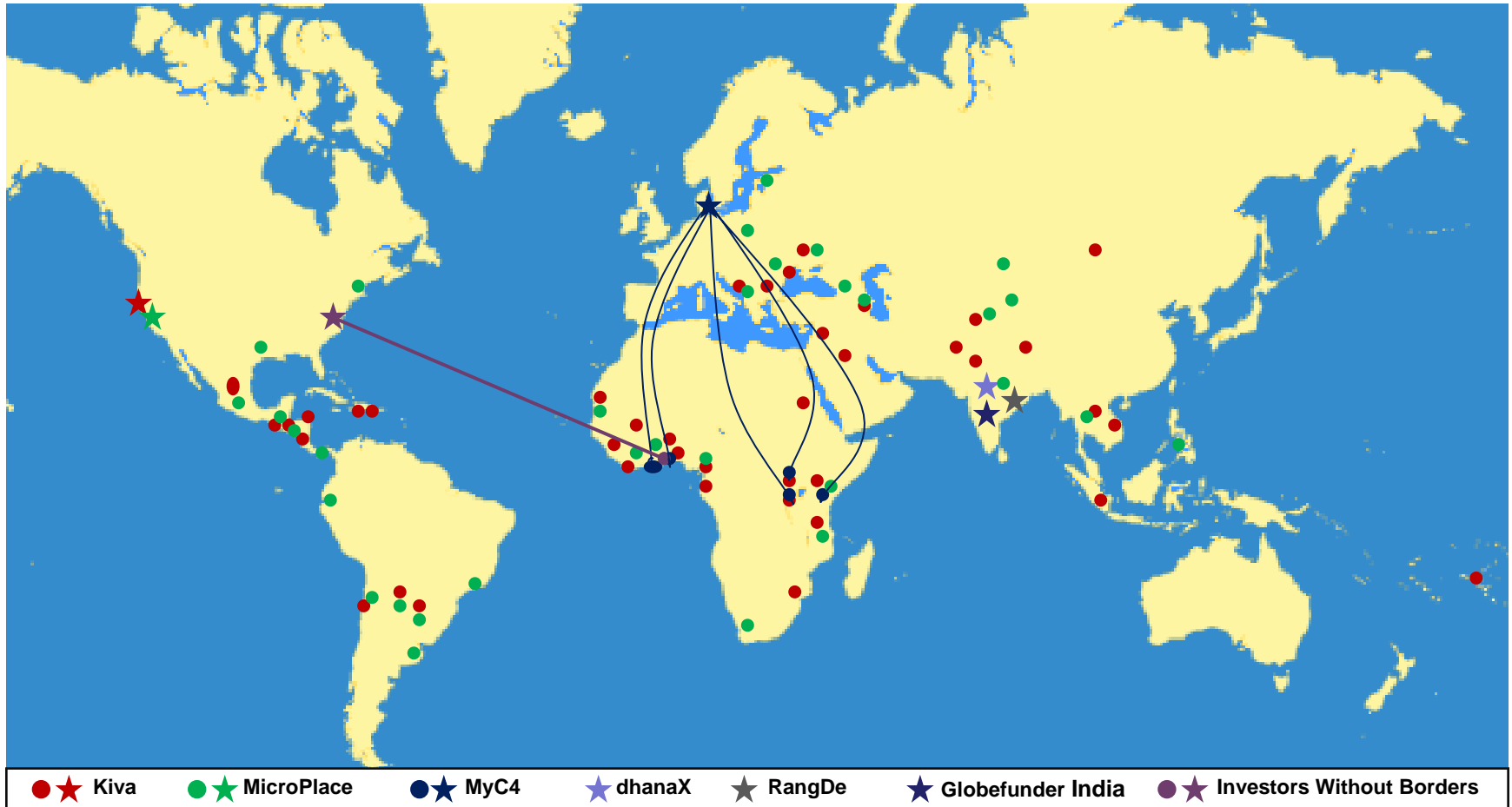
Developing Economies

- ❖ Kiva launched in November 2005
- ❖ 5 online platforms launched: dhanaX (India), Kiva (Global), MicroPlace (Global), MyC4 (Africa), and RangDe (India)
- ❖ 2 more expected soon: Globefunder (India) & Investors Without Borders (Ghana) :
- ❖ ~\$60 million have been lent to micro and small business in the developing world via P2P platforms
- ❖ ~70,000 loans made with P2P funding



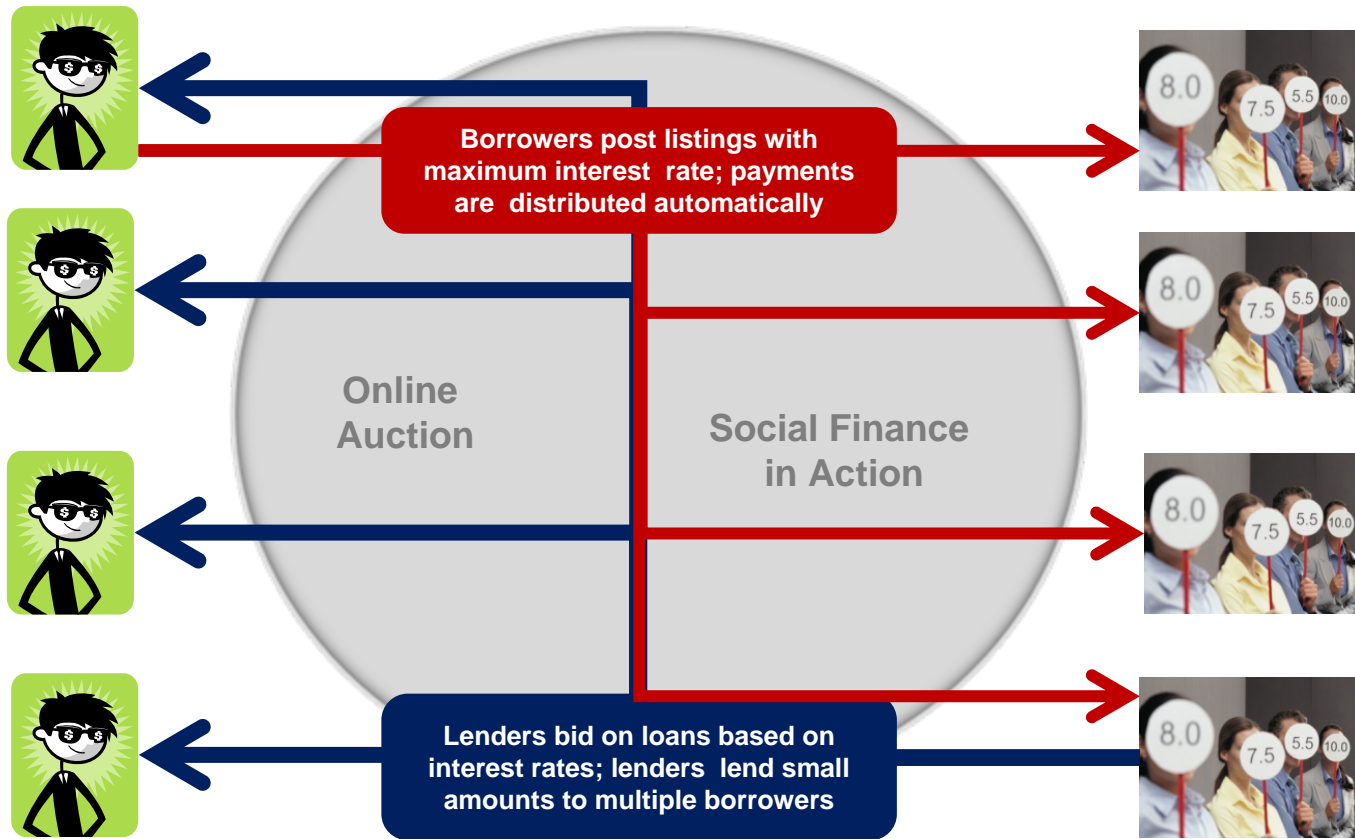
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Reach of Microfinance Oriented Platforms



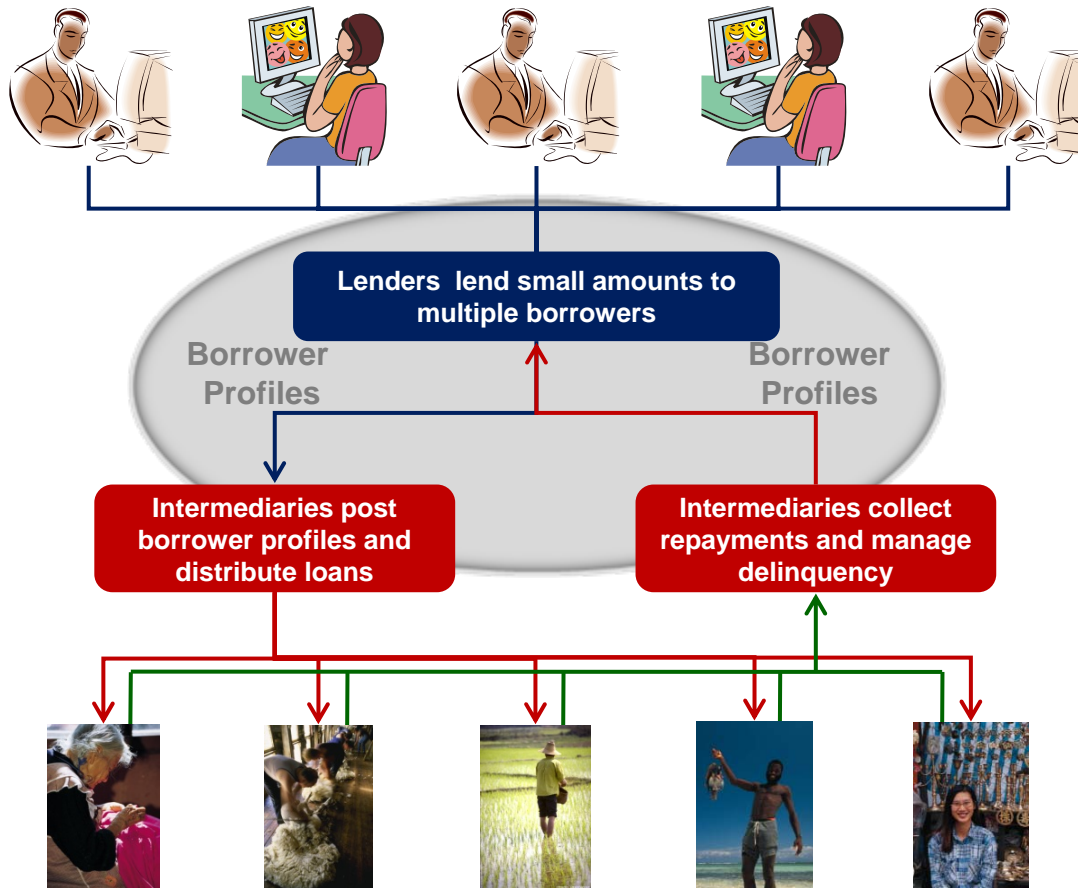


The Direct P2P Model



Note: Includes most developing country P2P platforms. Some variations do not use an auction system but set the rates and terms themselves.

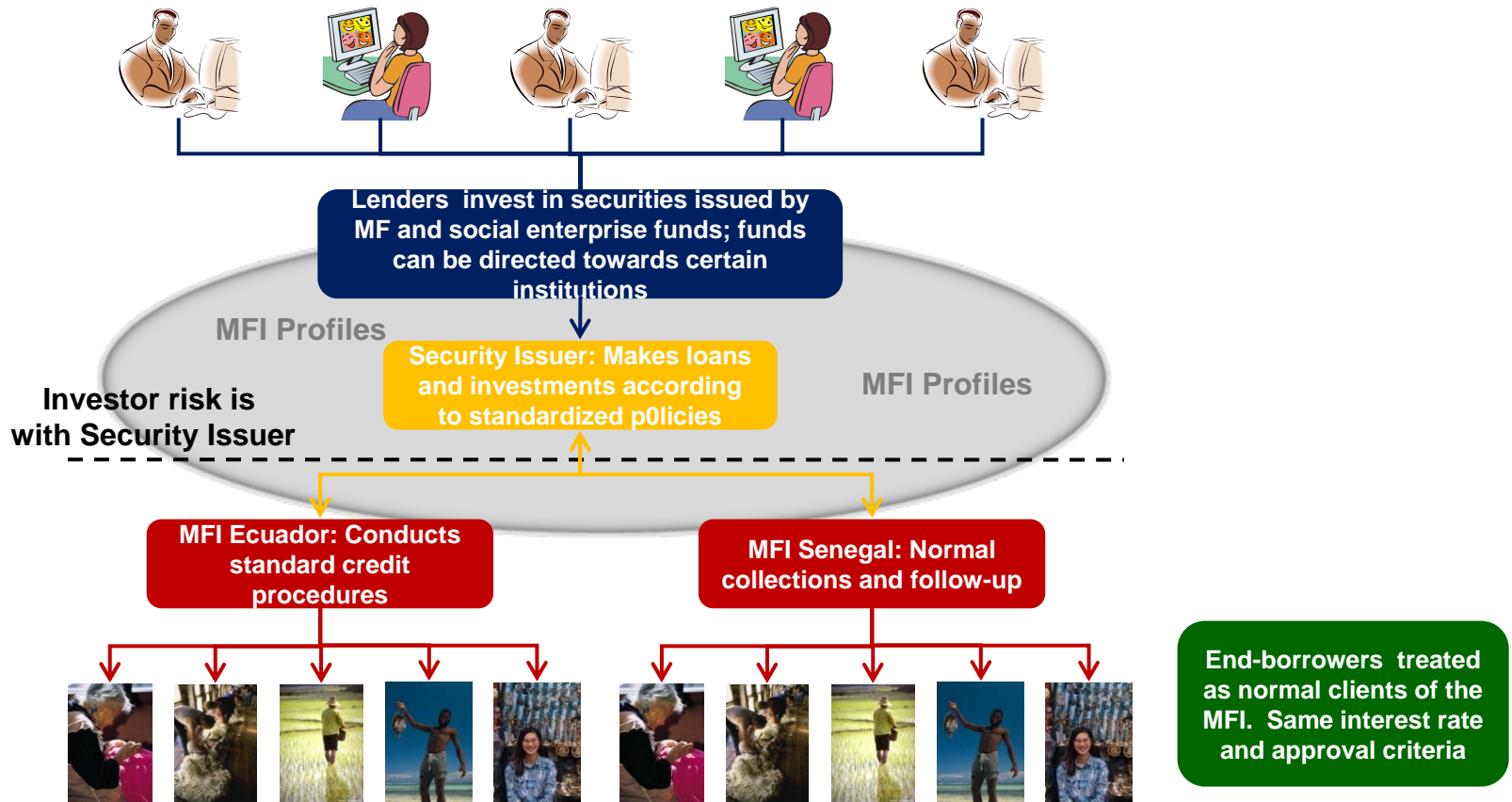
The Intermediary P2P Model



Borrowers are subject to Intermediary due diligence and credit processes

Note: Includes DhanaX, Investors Without Borders, Kiva, MyC4, and RangDe. Interest rates and terms are usually set by the Intermediary or the P2P.

The MicroPlace Model



Note: Return to investors set by security issuer; interest rate to borrower set by MFI. Investor can direct funds towards a particular MFI but credit risk is with the Security Issuer which generally has a portfolio of investments in diverse MFIs.

Democratizing Financial Intermediation for the Investor

❖ Benefits:

- Easy access to new type of investment
- Small investment minimums
- Easy diversification on platforms
- Higher interest rates than savings and CDs
- Feel good about “doing good”
- Personal connection with borrower

❖ Drawbacks:

- Higher risk investment
- Difficult to check borrower information
- Personal sentiment may negatively influence investment

Democratizing Borrower Access to Finance

❖ Benefits:

- Increase access to finance for the “unbanked”
- Lower interest rates
- Alternative source of capital during economic downturns
- Opportunity to escape debt-cycle (i.e. credit cards or moneylenders)
- Simpler loan terms and limited collateral requirements
- Easy application and disbursement
- Satisfaction of paying interest to a person not a bank

❖ Drawbacks:

- Privacy could be compromised online
- Loan amounts are limited
- Generally more borrowers than lenders on platforms



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Impact on the Microfinance Industry

		INTERMEDIARY P2P MODEL						INVESTMENT FUND
		dhanaX	Globe-funder	IWB	Kiva	MyC4	RangDe	MicroPlace
BENEFITS	Expansion of Funding Sources	✓	TBD	TBD	✓✓✓	✓	✓	✓✓
	Diversification of Funding	✓	✓	TBD	✓✓	✓	✓	
	More inelastic supply of funds	TBD	TBD	TBD	✓	✓	TBD	✓
	Cheap source of funding		TBD	TBD	✓✓✓	✓	✓	✓
	Target smaller MFIs	✓	TBD		✓✓		✓✓	✓
	Raises awareness of microfinance	✓	✓	✓	✓✓✓	✓✓	✓	✓✓
DRAWBACKS	Hidden costs to MFIs	✓	✓✓		✓✓		✓✓	
	Short-term, unpredictable financing	✓	TBD	TBD	✓✓		✓✓	
	Risk of Moral Hazard in Client Selection	✓	✓	✓	✓	✓	✓	



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Constraints to Scalability

- ❖ Demand-side challenges
 - Finding the right message to attract investors
 - Breadth of product offering attractive to investors
- ❖ Supply-side challenges
 - Sourcing borrowers
 - Creating partnerships with intermediaries
- ❖ Complex regulatory environments
- ❖ Transparency
 - Accuracy of borrower information
 - Openness regarding fees and interest rates
 - Easy to use and accurate reporting
- ❖ Foreign exchange risk



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Thank you!

Access the complete Peer-to-Peer Lending microREPORT,
at www.microlinks.org

A screencast of this presentation will be available shortly at
www.microlinks.org/afterhours

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